BEFORE THE

SURFACE TRANSPORTATION BOARD

_____

STB EX PARTE NO. 658

THE 25TH ANNIVERSARY OF THE STAGGERS RAIL ACT OF 1980:
A REVIEW AND LOOK AHEAD

_____

COMMENTS OF
MONTANA WHEAT & BARLEY COMMITTEE
COLORADO WHEAT ADMINISTRATIVE COMMITTEE
IDAHO BARLEY COMMISSION
IDAHO WHEAT COMMISSION
NEBRASKA WHEAT BOARD
OKLAHOMA WHEAT COMMISSION
SOUTH DAKOTA WHEAT COMMISSION
TEXAS WHEAT PRODUCERS BOARD
WASHINGTON WHEAT COMMISSION
NATIONAL ASSOCIATION OF WHEAT GROWERS

_____

I. INTRODUCTION

The MONTANA WHEAT & BARLEY COMMITTEE, COLORADO WHEAT ADMINISTRATIVE COMMITTEE, IDAHO BARLEY COMMISSION, IDAHO WHEAT COMMISSION, NEBRASKA WHEAT BOARD, OKLAHOMA WHEAT COMMISSION, SOUTH DAKOTA WHEAT COMMISSION, TEXAS WHEAT PRODUCERS BOARD, WASHINGTON WHEAT COMMISSION AND NATIONAL ASSOCIATION OF WHEAT GROWERS (known as Wheat & Barley Commissions) welcomes the opportunity to file comments on the past, present and future of rail regulation. This is a focused effort by the Wheat & Barley Commissions in this proceeding because of the importance that federal regula-

tory oversight of railroads or lack of it, bears on the marketing and transportation of wheat and barley. Your Wheat and Barley Commissions have filed together and participated in various Ex Parte proceedings in the past and they welcome the opportunity to address a broad range issues in this proceeding. The past, present and future of regulatory oversight affects the daily lives of this nation's wheat and barley producers.

II. IDENTITY AND INTEREST OF WHEAT & BARLEY COMMISSIONS

The Wheat & Barley Commissions represent wheat and barley producers in the major wheat and barley producing areas of the United States. They represent the majority of wheat and barley production. The Wheat & Barley Commissions are charged with representing the interests of wheat and barley producers in the marketing of their grains both domestically and internationally. A vast majority of the wheat and barley producers represented by the Wheat & Barley Commissions are captive to rail carriers for significant portions of their freight shipments. The Wheat & Barley Commissions also concur in the statement in this proceeding filed by the Alliance for Rail Competition. There will be many participants in this proceeding covering a whole host of issues and the Wheat & Barley Commissions would like to focus on a couple of issues for your consideration as opposed to filling the pages with a multitude of issues.

III. WHEAT & BARLEY PRODUCERS ARE THE ONES WHO BEAR THE FREIGHT CHARGES IN THE TRANSPORTATION OF GRAIN

For the layman, a simplistic discussion of how wheat is marketed will illustrate the product flow and the importance that transportation rate levels play as a

price determinant of agricultural commerce. Wheat is sold by growers through local country elevators or grain sub-terminals located in the various states and subsequently transferred to merchandisers and exporters. The wheat is delivered by a farm producer to a local elevator. The producer is given the Grain Exchange price (basis), less rail transportation charges, less deduction for elevation and margin. For example, if the price of wheat at the market is $4.00 and the transportation price is $1.00 and elevation is $.15, the farm producer would receive $2.85 for his wheat. *Thus, the farm producer bears the transportation costs of moving the wheat to market*. The grain merchandiser pays the railroad, but the farm producer is the bearer of freight rates. There are many grain companies that may profess to paying the freight bills, but the party that bears the freight charges are the ones this Board should be protecting in the marketplace.

For the farm producer, the cost of transporting grain can represent as much as one third (1/3) the overall price received for the grain. The key to understanding the uniqueness of the farm producers plight is to understand: unlike virtually every other industry, the farm producers bear the freight charges and cannot pass them on to any other party in the distribution chain, and yet the farm producer does not physically pay the freight charges.

IV. WHEAT & BARLEY PRODUCERS CONTINUE TO EXPERIENCE SUB-STANDARD SERVICE AND DOMINEERING BEHAVIOR FROM CLASS I RAILROADS

The wheat and barley producers are experiencing generally poor service, high rates and business decorum from the nation's railroads that shifts from indifference to superciliousness. Why? With each successive merger and thus ever greater concentration of rail economic power, there is ever greater level of disconnection between railroad marketers and the rail customer. Recently a major railroad increased the agricultural rates to a plant by 40%. The company owning

the plant said the increased rates will ruin the plant's ability to stay in business (a business that has been attendant to the subject railroad for over 30 years) and the reply of the railroad was "do what you have to do." In another instance, a rail customer needed to negotiate a rate to bring a new plant on line, and the attendant railroad cancelled the long-standing published tariff rate in order to force the captive rail customer to deal with much higher rail rates in the form of a confidential contract. Many farm merchandisers live in fear of railroad reprisals if they are singled out for supporting any changes in the status quo. This Board should be extremely concerned that the railroads they are charged with overseeing continue to utilize their federally granted economic power with such heavy handed conduct.

V. STAGGERS RAIL ACT AS PASSED BY CONGRESS IN 1980 SOUGHT TWO MAJOR OUTCOMES BUT THE REGULATORS HAVE CHOSEN THAT ONE HAS PRIORITY OVER THE OTHER

It is the view of the Wheat & Barley Commissions that when the Staggers Rail Act was passed Congress was seeking two major outcomes – 1.) by focusing on deregulation, the charge was to produce a stronger rail industry that was, at that time, plagued with multiple bankruptcies, and 2.) protecting of the captive rail customers from potential abuse that might occur due to decreased regulatory oversight and the inevitable consolidations that would occur in the future. Indeed, increased rail-to-rail competition was called for by Congress in the Stag-

gers Rail Act. In Title 49, Subtitle IV, Part A, Chapter 101: Section 10101. - Rail transportation policy the word ‘competition’ is utilized in four of the fifteen parts.

1. to allow, to the maximum extent possible, competition and the demand for services to establish reasonable rates for transportation by rail;
4. to ensure the development and continuation of a sound rail transportation system with effective competition among rail carriers and with other modes, to meet the needs of the public and the national defense;
5. to foster sound economic conditions in transportation and to ensure effective competition and coordination between rail carriers and other modes;
6. to maintain reasonable rates where there is an absence of effective competition and where rail rates provide revenues which exceed the amount necessary to maintain the rail system and to attract capital;

However, the ICC and later the STB, developed a view that developing a stronger rail system financially somehow became a trump card over protecting captive shippers. In essence, the Commission and the Board used concepts such as revenue adequacy and embracing lessening competition as a trump card in rate and service cases when faced with calls from rail customers to mandate corrective rail action.

The results are clear. The trumping of the captive shipper protections by ever-present financial concerns of the ICC/STB has resulted in far less competition. The ICC/STB have approved rail merger after rail merger resulting in the most massive concentration of rail power over rail customers since the beginning

of railroads in this country over 100 years ago. The ICC then followed this approval of increased concentration with a series of rulings such approval of bottleneck rates, terminal access restrictions and paper barriers which effectively shut off large portions of the country to the effects of rail competition following the mergers of major carriers.

More results - implementation of the relevant provisions of the 1980 Staggers Rail Act were not coupled with equal enforcement standing of shipper provisions by the ICC and STB and that has resulted in less competition and unparalleled concentration.

The farm producers continued to be concerned that rail shippers (the parties bearing the freight rates) today are facing the effects of increasing railroad monopoly and market power coupled with ineffective rail regulation and a system that allows only baseball and the railroads to have anti-trust protection.

We know of no other industry with the freedom that major railroads enjoy pursuing their own self-interest without fear of regulatory, legal or competitive challenges. For these reasons, the status quo is unacceptable, even if railroad financial health has improved. Unrestricted railroad monopoly power does not serve the public interest.

The most pressing question and the heart of this Ex Parte exploration is what is best to address the public interest. After all, protecting the public interest is clearly what Congress desires when it makes changes to the regulatory scheme. In our mind, every rail customer - the public, needs a competitive rail transportation system that provides fairly priced, safe and reliable service.

If we just review the results of the ICC/STB merger policy for a moment. Look at the history of the past several rail mergers. They have not significantly improved service. They have not increased or even maintain existing competition levels in the market place. They have not resulted in lower rates. They have

not resulted in increased efficiency. They have resulted in service disruptions, closed gateways and increased transportation costs for the ever increasing base of rail customers. The costs associated with service disruptions go far beyond the loss of revenue to the rail customer. Loss of business to the rail customer equates to loss of employee wages, lost sales and market share, increased trucking which costs local and state government, and attendant local air pollution. These increased costs and losses ripple throughout the local economies. The rail customers are not the ones who should be paying for these rail mergers. The railroads merge to increase revenues and their bottom lines.

From the captive rail customer's eyes today, the railroad industry is a rail system fraught with a series of continuing service problems that go on year after year; customer suffering, and rate gouging. As previously stated, the reality, due to an overly consolidated rail industry, is the railroad industry is characterized by lack of competition among the nation's railroads; whole states and complete industries are captive to a single railroad; and there has been thousands of cases of market abuse testified to at various STB and Congressional hearings in the last several years.

VI. ENHANCEMENT OF COMPETITION MUST BE ATTENDED TO NOW BEFORE THE START OF THE END GAME

The Board, in Ex Parte 582 Sub 1, was correct in their initial view that competition must be enhanced to serve the public interest. The railroads in their comments in the same proceeding wanted this Board to <u>not</u> consider 'downstream' effects in evaluation of future railroad mergers. Given that a two monopoly continent-wide railroad system will be the inevitable result of the next round of mergers, to not evaluate all downstream effects even if such evaluation involves speculation of future proposed mergers is too important not to be considered. The proposed look at downstream effects is what has been missing from national rail merger policy for the last 30 years. Surprises, we, the rail customers in this

nation, are already faced with two railroads controlling thousands of rail customers. West of the Mississippi River, we have two major railroads controlling the lion's share of the traffic and east the Mississippi River, the same story. The public interest requires that the STB meet the needs of the rail customers by finally becoming a proactive force for enhancing competition. If the STB doesn't become proactive soldiers for enhanced competition, there may be nothing left for the STB to oversee. There is, in the market place, growing and continuing evidence of market power abuse and continuing abysmally poor levels of customer's service. The STB needs to be clear on its rules. The courts require it.

The Wheat and Barley Commissions note that at least one Class I railroad achieved revenue adequacy in 2004, and more may do so in 2005, even under revenue adequacy standards that clearly favor railroads looking for special consideration in rate cases and rulemaking proceedings. Things have changed today in the railroad industry. No longer is there excess capacity. No longer do railroads tend to compete on price. Constrained Market Pricing does not have the relevance that it did in a railroad excess capacity world.

The current regulatory scheme is prefaced on the belief that railroads need to gouge the captive shippers in order to achieve revenue adequacy; that two railroads will always compete in an area; and in which railroads will always strive for more and more traffic. What if the two railroads in an area decide not to compete for business but just divide up the business that is available? What if a major railroad decides that less traffic on the system will lead to more profitability and starts driving off traffic in captive areas? What if the railroads of today consciously develop methods of pricing and competition that allow them to continue to increase prices? What if the railroads do not chose to compete if an Industry puts up the money for a build-out or build-in? Is the current regulatory approach which does not focus on the new realities facing the rail dependent industries served by the railroads, serving the public interest?

These developments, as well as the elimination of excess rail capacity and the demonstrated falsity of claims that rates cannot be increased on the traffic of

non-captive shippers, provide additional grounds for new approaches to rail regulation, and for new measures to enhance rail competition.

The Board therefore needs to analyze alternatives to business as usual.

VII. DISCUSSION

The Wheat & Barley Commissions recognize that reasonable people may be able to differ as to the wisdom of some ICC and STB decisions, and that some decisions were well intended.

After 25 years of ICC and STB rulemakings and adjudications that have produced very few protections for captive shippers, and no safe havens, and a railroad industry that is moving towards unprecedented dominance in the market place, a new regulatory environment vision needs to formulate. It should come as no surprise that most captive shippers regard recourse to the STB as, at best, a waste of time and effort, and at worst, a costly exercise in futility which is likely to lead to railroad retaliation than to reasonable rates or service. See e.g., GAO Report No. 99-46, "Railroad Regulation – Current Issues Associated with the Rate Relief Process," which found that 70% of shippers "believe the time, complexity and costs of filing complaints are barriers that often preclude them from seeking rate relief." (Report at 4).[1]

If one takes a look at recent Board actions, they have changed the rules on rail customers. It is the duty of all common carrier railroads to provide and furnish transportation upon reasonable request. Further, all railroads have a common law duty to provide car service on reasonable request, and that includes "shippers located on branch or lateral lines of railroad, and [such shippers] are entitled to the same kind of treatment to those whose business is on the main line of the railroad."[2]. The Congress has made the common law duty to provide service on reasonable request, without undue discrimination, to all shippers a duty of national concern. In short common carrier railroads are obligated to pro-

[1] See also Report at 9: "Some shippers and their associations also contend that the improvements already made to the rate complaint process are at best incremental steps and point to a lack of competition in the railroad industry as the underlying problem."

[2] Chicago, R.I & P. Ry. Co. v. Sims, 256 S.W.33

vide adequate transportation service on reasonable request. The railroad is expected to inform itself of shipper needs so that it can invest in sufficient transportation facilities to meet those needs[3]. While a temporary car shortage can be a defense, it is a defense only if the railroad has adopted a rule for distribution of available cars without discrimination. Alternatively if a rule has not been developed, the distribution is made without undue discrimination.

The STB has been allowing carriers to shift cars from one class of service based upon the belief that the other service provides more efficiency = better turnarounds. This overt sanctioning of discrimination by the STB has led, on the prairies, to the have and the have nots among grain facilities. But the law of many years suggests that car supply must be made without undue discrimination and for many years until recently that was how car distribution was allocated.

IX. WHERE TO FROM HERE?

On the positive side, we see that the Board has also adopted more open and transparent procedures. However, more oral arguments, hearings and public voting conferences provide little consolidation if shippers are consistently denied relief.

The 1980 Staggers Rail Act was clear and the Wheat & Barley Commissions embrace its concepts. They were clear: deregulate, improve the financial standing of the railroad industry and all the while protect the shippers that will be disadvantaged by these deregulatory efforts.

The Board should start to explore rate regulation which recognizes the status of captivity. The Wheat & Barley Commissions can show rate levels in each state of 200%, 250%, 300% and in some cases as high as 400+% of revenue to variable cost. How much is too high? Are rates above 300% excessive? Faced with the effects of a railroad monopoly that was withering a key element of the state's economy, Montana filed a class-action and formal complaint pursuing the *McCarty Farms* case for **17 years**, wherein the *ICC on December 14, 1984*

[3] Illinois Central Railroad Co. v. River & Rail Co. & Coke Co., 150 S.W. 641: Anderson v. Chicago, M. & St. P. Ry. Co., 175 N.W. 246

found that the BN had market dominance and that its rates were unreasonable. The Administrative Law Judge (ALJ) further found that the rates were higher than 300% of variable cost! Yet, this Board in 1997, found that these rates were not excessive!

It is time for new approaches to be explored by this Board. Over at FERC, which regulates large capital intensive industries (pipelines), their regulatory approach is yielding a system of regulatory oversight that is embraced by both carriers and shippers. The system adjudicates thousands of cases with dispatch and without resorting to CPM pricing or differential pricing based upon captivity. It is time that this Board explore new approaches to a railroad system that is down to four dominant carriers controlling over 90% of the traffic and revenues.

Wheat & Barley Commissions predict that the Class I railroads' comments in this proceeding will state that any change in any of these policies will condemn the railroad industry to financial ruin. They have been stating the same battle cry for years and it has been nonsensical for years. To the extent that reduced capacity in the transportation system as a whole leads to higher rates and charges on <u>all</u> rail traffic, captive and nonjurisdictional, the railroad industry no longer needs more and higher captive shipper rates, or the anticompetitive conduct that supports such rates.

In any event, the choice facing the Board is not between minimizing rail-to-rail competition and maximizing rail-to-rail competition, rather the choice is looking at cases that allow a system of regulatory oversight that fosters competition.

We come to a time when public policy must be reexamined.

No one has a greater interest in sound railroads than shippers, perhaps not even the railroads themselves. The Wheat & Barley Commission seek a rail system and regulatory scheme that is predicated upon three guiding ideas:

1) A SAFE, GROWING AND FINANCIALLY STRONG RAIL INDUSTRY
2) *ELIMINATION OF MONOPOLISTIC PRACTICES BY FURTHERING THE DIRECTION DEVELOPED IN THE STAGGERS RAIL ACT*
3) COOPERATIVE INNOVATION AND CREATIVITY DRIVEN BY RAIL-TO-RAIL COMPETITION

We simply do not believe that this mighty and historic railroad industry cannot function in a competitive American marketplace, as do all other businesses in the country.

IV. CONCLUSION

The American market place and world competitiveness is changing, and the ICC/STB regulatory regime established with railroad revenue adequacy as its top priority no longer comports with sound law, economics or policy.

Change is needed, indeed broad change. Will railroads and rail customers have to adapt to a new regulatory environment? Of course, just as we all have had to adapt to conditions dictated by the free markets and the global economy. We believe it is unhealthy to have railroads operate in the current federally sheltered environment. This artificial habitat is unhealthy for shippers…and unhealthy for railroads too.

Respectfully submitted,

Terry C. Whiteside
Registered Practitioner
Whiteside & Associates
3203 Third Avenue North, Suite 301
Billings, Montana 59101
(406) 245-5132